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Computing the "Kiddie Tax" for Children Under Age 14

Investment income over $1,300 earned by a child under age 14 is taxed at the child's parent's top tax rate. The child's parent or legal representative generally makes this tax computation, which is nicknamed the "kiddie tax."

The kiddie tax applies only to investment income, such as interest, dividends, rents, royalties and profits on the sale of property. Income from wages and self-employment is not subject to the kiddie tax.

As the child's parent, you generally must use Form 8615 to report the child's income and compute the tax which is reported on the child's personal income tax return; *see* ¶24.4. The Form 8615 computation has no effect on the treatment of items on your own return or on your tax computation. You may instead elect on Form 8814 to report the child's investment income on your own return, provided the child received only interest and dividend income. This election is generally not advisable. If you elect on Form 8814 to report the child's investment income on your own return, your adjusted gross income will increase and this could adversely affect your right to claim various deductions; *see* ¶24.5.

If you are married but file separately, the parent with the larger amount of taxable income is responsible for the kiddie tax computation. If parents are divorced, separated, unmarried, or living apart for the last six months of the year, the parent who has custody of the child for the greater part of 1996 computes the tax. If a child cannot get tax information directly from a parent, the legal representative of the child may ask the IRS for permission on Form 8615.

¶24.1 Filing Your Child’s Return

To discourage substantial income splitting of investment income between parents and minor children, the tax law has complicated income reporting for parents and children by—

1. Taxing a child’s investment income over $1,300 at the parent’s top bracket if the child is under 14 years of age at the end of the taxable year; *see* ¶24.3.
2. Barring a dependent child from claiming a personal exemption on his or her own tax return.
3. Limiting the standard deduction to $650 for a dependent child who has only investment income; *see* ¶13.5.

Does your child have to file? For a child who can be claimed as a dependent, the income filing threshold is generally $650. If your dependent child has gross income (earned and investment income) of $650 or less for 1996, he or she is not subject to tax and does not have to file a tax return.

A 1996 return must be filed for a dependent child with gross income of more than $650, but there is this exception: If a dependent child has salary or other earned income but no investment income, a return does not have to be filed unless such earned income exceeds $4,000 in 1996.

Although a dependent child may not claim a personal exemption on his or her 1996 tax return, the child is allowed to claim a $650 standard deduction. A dependent child with earned income over $650 may claim a standard deduction up to those earnings, but no more than the basic standard deduction, which is generally $4,000; *see* ¶13.1.

How to file for your child. If your child was under age 14 as of January 1, 1997, and had investment income of $1,300 or less, follow the regular filing rules and use either Form 1040EZ, 1040A, or Form 1040 to report the child’s income and deductions. The “kiddie tax” compution does not apply, so all of the child’s income will be taxed at his or her own tax rate. If your child is unable to sign his or her tax return, you must do so; *see* ¶1.11.

If your child’s investment income exceeded $1,300, the kiddie tax computation applies; *see* ¶24.3. Form 8615 must be filed to compute the kiddie tax unless your child’s only income is interest and dividends and you elect to report your child’s investment earnings on your own return as discussed at ¶24.5. On Form 8615 you must provide your tax identification number and taxable income. Form 8615 is attached to the child’s tax return; *see* ¶24.4.

If your child was age 14 or older as of January 1, 1997, your child should file Form 1040EZ, 1040A, or 1040, depending on the type of income and deductions he or she has. The special kiddie tax rules do not apply.

Child’s AMT liability. A child who has substantial tax-exempt interest, tax preferences, or tax adjustments subject to the alternative minimum tax must compute tentative AMT liability on Form 6251; *see* Chapter 23. However, AMT liability for a child under age 14 is reduced or eliminated if that child’s parent or sibling (also under age 14) has regular tax liability exceeding tentative minimum tax liability. This AMT limitation for children under age 14 is figured on a worksheet included in the Form 6251 instructions. The worksheet allocates the proper AMT between the parent and the children. The child’s AMT cannot exceed the extra tax that the parent would pay if the child’s tentative minimum tax liability, plus regular tax, was added to the parent’s own.

¶24.2 Children Not Subject to the “Kiddie Tax”

For 1996 returns, the “kiddie tax” computation applies only to a child who was under age 14 on January 1, 1997, and who had investment income for 1996 exceeding $1,300. The computation does *not* apply to—

- A child who was 14 years old or over on January 1, 1997.
- A child under age 14 who had no investment income or whose 1996 gross investment income was $1,300 or less. The kiddie tax computation applies only to investment income exceeding $1,300. Furthermore, children who itemize deductions may in some cases exempt more than $1,300 from the computation; *see* ¶24.3.
- A child under age 14 if neither parent was alive at the end of 1996.

EXAMPLES

1. At the end of 1996, your son is age 14. He has interest income of $1,400 and salary income of $950 from his part-time job. His standard deduction is $950, the greater of earned income and $650. No personal exemption may be claimed. Assuming he has no itemized deductions, taxable income is $1,400 ($2,350 gross income – $950 standard deduction). The kiddie tax computation based on your top rate does not apply because your son is at least age 14 at the end of the year.
2. In 1996, your five-year-old daughter has interest income of $800. Taxable income of $150 is subject to tax at her own tax rate.

Interest income	$800
Less: standard deduction	650
Taxable income	$150

The kiddie tax computation does not apply because investment income does not exceed $1,300.

¶24.3 Children Under Age 14 Subject to the “Kiddie Tax”

The “kiddie tax” computation for 1996 returns applies to a child who—

- Was under age 14 on January 1, 1997;
- Had either parent alive at the end of 1996; *and*

- Had investment income for 1996 exceeding $1,300. For a child who has itemized deductions of more than $650 that are directly connected to the production of investment income, the $1,300 exemption is increased, as explained below.

Figuring kiddie tax on child's or parent's return. The kiddie tax computation is generally made on Form 8615, which must be attached to your child's return. A sample Form 8615 is on page 378. However, if the only income of your child who is under age 14 is interest and dividends and other tests are met, you may elect on Form 8814 to include your child's investment income on his or her own tax return, instead of computing the kiddie tax on Form 8615; *see* ¶24.5.

Kiddie tax on Form 8615 applies to investment income exceeding $1,300 floor. If your child files his or her own return and the "kiddie tax" is computed on Form 8615, your top rate applies to *net investment income.* For purposes of this rule, *net investment income* equals gross investment income minus $1,300 if your child does not itemize deductions on Schedule A. Thus, if your child does not itemize, the first $1,300 of investment income is exempt from the special computation. Investment income exceeding $1,300 is considered net investment income subject to the special computation; *see* Example 3 in the next column.

Include as gross investment income all taxable income that is not compensation for personal services. Include interest income, unless it is tax-exempt interest, dividends, royalties, rents, and profits on the sale of property. Payments from a trust are also included to the extent of distributable net income. Most accumulation distributions received by a child from a trust are not included because of the minority exception under Code Section 665(b) for amounts accumulated before age 21. Income in custodial accounts is treated as the child's income and is subject to the kiddie tax computation.

Investment earnings on all of your child's property must be considered, even if the property was a gift from you or someone else, or if the property was produced from your child's wages, such as a bank account into which the wages were deposited. The wages themselves, or self-employment earnings, are not considered.

If your child does itemize deductions, and has more than $650 of deductions that are directly connected to the production of investment income, the $1,300 floor is increased. The floor is $650 plus the directly connected deductions. If the directly connected deductions are $650 or less, the regular $1,300 kiddie tax exemption applies, as in Example 4 in the next column. Directly connected itemized deductions are expenses paid to produce or collect income or to manage, conserve, or maintain income-producing property. Only the part of the total expenses exceeding the 2% AGI floor may be deducted. These expenses include custodian fees and service charges, service fees to collect interest and dividends, and investment counsel fees. If, after you subtract the itemized deductions, your child's net investment income exceeds his or her taxable income, you apply the tax to the lower taxable income, rather than to the net investment income.

EXAMPLES

(In all the following Examples, assume the child is your dependent for 1996 and under age 14 on January 1, 1997.)

1. Child has interest income of $480 and no other income. The child has no income tax liability and does not have to file a return.

Interest income	$480
Less: standard deduction	480
	–0–

2. Child has interest and dividend income of $900 and no other income. A standard deduction of $650 may be claimed. The balance of $250 is taxed at the child's regular tax bracket. Form 8615 does not have to be filed and the kiddie tax computation does not apply since investment income does not exceed $1,300.

3. Child has dividend income of $1,800 and taxable income of $1,150, of which $500 is subject to the kiddie tax computation based on the parent's top tax bracket on Form 8615.

Figuring taxable income:	
Dividend income	$1,800
Less: standard deduction	650
	$1,150
Income subject to tax at parent's rate:	
Investment income	$1,800
Less: $1,300	1,300
	$ 500

An example of the actual Form 8615 computation is at ¶24.4. As an alternative to computing kiddie tax on $500 on Form 8615, the parent may elect to report the child's dividend income on his or her own return; *see* ¶24.5.

4. Child has $300 of wages and $1,750 of dividends and interest income. On Schedule A, the child claims itemized deductions of $400 related to investment income after the 2% AGI floor. The child also has $400 of other itemized deductions. Itemized deductions of $800 are claimed; they exceed the $650 standard deduction.

Figuring taxable income:	
Total income	$2,050
Less: itemized deductions	800
Taxable income	$1,250
Income subject to tax at parent's rate:	
Investment income	$1,750
Less: greater of (1) $1,300 and (2) the sum of $650 and directly related expenses of $400	1,300
Net investment income subject to tax at parent's rate on Form 8615 (¶24.4); *see* ¶24.5 for parent's alternative election.	$ 450

¶24.4 Computing "Kiddie Tax" on Child's Return

If your child is subject to the "kiddie tax" under ¶24.3, the tax is computed on Form 8615, which is attached to his or her return, unless you make the parent's election at ¶24.5. Before your child's Form 8615 can be completed, your own taxable income must be determined. The amount to be entered on Form 8615 as the parent's taxable income depends on the parent's marital and filing status.

If the parents file a *joint return,* their joint taxable income is entered on Form 8615, along with the net investment income (¶24.3) of all their children under age 14. If the parents file *separate returns,* the larger of the parents' separate taxable incomes is used on the child's Form 8615.

Where parents are legally separated or divorced and custody of the child is shared, Form 8615 should be completed using the taxable income of the parent who has custody for the greater part of the year. If parents are married but living apart, and the custodial parent qualifies as unmarried under Test 1 at ¶1.10, that parent's taxable income is used on Form 8615. If the custodial parent is not considered unmarried, the income of the parent with the larger taxable income is used. If the custodial parent has remarried and files a joint return with a new spouse, their joint return taxable income is used on the child's Form 8615. If the parents were never married but they live together with the child, the income of the parent with the larger taxable income is used; if the parents live apart, the income of the parent with custody for most of the year is used on Form 8615.

More than one child subject to kiddie tax. You file a separate Form 8615 for each child and on each form net investment income of all the children subject to the tax is included. The computed tax is allocated to each of your children, according to his or her share of their combined net investment income. This computation is incorporated in the steps of Form 8615 and by following the order of the form, you will make the proper allocation.

As parents, the kiddie tax computation on Form 8615 does not affect your tax liability or how you compute any limitation on deductions or credits. For example, the addition of the child's net investment income to your taxable income on Form 8615 does *not* affect the adjusted gross income floors for purposes of figuring your deduction for IRA contributions, medical expenses, or miscellaneous expenses.

EXAMPLE

For 1996, Bill and Betty Brown each file Form 1040A. Bill, age 12, has dividend income of $2,100; Betty, age 10, has $1,500. They each claim a standard deduction of $650. Neither may claim a personal exemption because they are claimed as dependents by their parents, Tom and Lilli Brown. Bill's taxable income after claiming the standard deduction is $1,450. Betty's is $850.

Tom and Lilli Brown do not make the election (¶24.5) to report Bill's and Betty's dividends on their joint return. Forms 8615 are prepared and attached to the children's Forms 1040A, because each child is under age 14 and has more than $1,300 of investment income.

Tom and Lilli report taxable income of $52,000 on their 1996 joint return. They use the IRS tax tables to look up their tax (the tables are in the Tax Organizer, Part VIII of this book). The tax on $52,000 is $9,354. The special computation on Form 8615 does not increase their joint return tax; it determines only the amount of Bill's and Betty's tax.

As shown on page 378 on sample worksheets based on Form 8615, Bill's 1996 tax is $323 and Betty's 1996 tax is $155. If the special computation did not apply, Bill's 1996 tax would be $219 and Betty's tax would be $129. Thus, as a result of the special computation, the total tax bill for the children is increased by $130 ($478 – $348).

Estimating the kiddie tax in case of filing delay. If you are unable to file your return by April 15, 1997, the child's tax on Form 8615 may be based on an estimate. You may make a reasonable estimate of your taxable income on Form 8615 or may estimate the net investment income of children under age 14 if that information is not yet available. When you have the complete income details, file an amended return.

A reasonable estimate may be based on your 1995 taxable income and the 1995 investment income of the child. If a refund is due, the IRS will pay interest from April 15, 1997, or, if the return was filed late, from the filing date. If additional tax is due on the amended return, interest will be charged from April 15, but no penalty will be imposed.

¶24.5 Parent's Election To Report Child's Dividends and Interest

Instead of filing a separate return for your child (¶24.4) whose income is subject to the "kiddie tax," you may elect on Form 8814 to compute the kiddie tax on your return if all of the following tests are met:

- The child's income is only from interest and dividends (Alaska Permanent Fund dividends may be included);
- The total interest and dividends are over $650 but less than $6,500;
- Estimated tax payments were not made in the child's name and Social Security number for 1996, and there was no overpayment from the child's 1995 return applied to his or her 1996 estimated tax; and
- The child was not subject to 1996 backup withholding.

By making this election, and following the steps of Form 8814, you include in your income the child's interest and dividends to the extent they exceed $1,300. You also figure an additional tax equal to the smaller of $97.50 and 15% of your child's income over $650.

If parents are divorced, separated, unmarried, or living apart for the last six months of the year, the parent whose taxable income would be taken into account on Form 8615 (¶24.4) is the parent who may elect to report the income on his or her own return.

In figuring whether you owe alternative minimum tax (AMT), you must include as a tax preference item interest income your child receives from specified private activity bonds; *see* ¶23.6 and Form 6251 instructions.

Should you make the election? There is no advantage in making the election, except to skip the paperwork involved in preparing a return in the child's name or returns in your children's names. If you consider this an advantage, you may want to make the election. It may be preferable to take the time to prepare the child's return to keep the child's tax accounting separate from yours. Including the child's income as your own increases your AGI, which may create these disadvantages:

- Subject you to the exemption phaseout (¶22.15) and 3% reduction computation (¶13.8) for itemized deductions.
- Make it more difficult to deduct job expenses and other miscellaneous itemized deductions, which are subject to a 2% AGI floor (¶19.1), and medical deductions, subject to a 7.5% AGI floor (¶17.1).
- Limit a deduction for IRA contributions under the phase-out rules (¶8.4).
- Limit your ability to claim the special $25,000 rental loss allowance under the passive activity rules (¶10.2).
- Increase local and state tax liability.

Finally, if you elect to report the child's income on your own return, you may not claim any deductions that your child would have been able to claim on his or her return such as investment expenses or a penalty on premature withdrawals from a savings account. On the other hand, reporting your child's interest or dividends increases your net investment income, which may allow you to claim a larger deduction for investment interest; *see* ¶15.10. Also, your ceiling for charitable donations may be increased. If you plan to report your child's income on your 1997 return, provide for the tax in your estimated tax payments or withholdings during 1997.

EXAMPLE

Woodrow, age 10, received $2,000 of interest income in 1996. He has no other income and is not subject to backup withholding. No estimated tax payments were made in his name. His parents elect on Form 8814 to include his interest income on their 1996 tax return instead of filing a return for him. They include $700 of the interest ($2,000 – $1,300 floor) on Line 21 (other income) of Form 1040. They also add $97.50 to their tax on Line 38 of Form 1040 and indicate that the amount is from Form 8814.

Form 8615–Worksheet

Child's name shown on return: Betty Brown — Child's social security number: X10 : 00 : 1111

A Parent's name (first, initial, and last). Caution: See instructions on back before completing: Tom Brown — B Parent's social security number: XXX : 11 : 1X11

C Parent's filing status (check one): ☐ Single ☑ Married filing jointly ☐ Married filing separately ☐ Head of household ☐ Qualifying widow(er)

Step 1	**Figure child's net investment income**		
1	Enter child's investment income, such as taxable interest and dividend income. See instructions. If this amount is $1,300 or less, **stop**; do not file this form	1	1,500
2	If the child DID NOT itemize deductions on Schedule A (Form 1040 or Form 1040NR), enter $1,300. If the child ITEMIZED deductions, see instructions	2	1,300
3	Subtract line 2 from line 1. If the result is zero or less, **stop**; do not complete the rest of this form but ATTACH it to the child's return	3	200
4	Enter child's **taxable** income from Form 1040, line 37; Form 1040A, line 22; Form 1040NR, line 36	4	850
5	Enter the **smaller** of line 3 or line 4 ►	5	200
Step 2	**Figure tentative tax based on the tax rate of the parent listed on line A**		
6	Enter parent's **taxable** income from Form 1040, line 37; Form 1040A, line 22; Form 1040EZ, line 6; Form 1040NR, line 36; Form 1040NR-EZ, line 13. If the parent transferred property to a trust, see instructions	6	52,000
7	Enter the total net investment income, if any, from Forms 8615, line 5, of ALL OTHER children of the parent identified above. **Do not** include the amount from line 5 above	7	800
8	Add lines 5, 6, and 7	8	53,000
9	Tax on line 8 based on the **parent's** filing status. See instructions. If from Capital Gain Tax Worksheet, enter amount from line 4 of that worksheet here ►	9	9,634
10	Enter parent's tax from Form 1040, line 38; Form 1040A, line 23; Form 1040EZ, line 10; Form 1040NR, line 37; Form 1040NR-EZ, line 14. If from **Capital Gain Tax Worksheet**, enter amount from line 4 of that worksheet here ►	10	9,354
11	Subtract line 10 from line 9. If line 7 is blank, enter on line 13 the amount from line 11; skip lines 12a and 12b	11	280
12a	Add lines 5 and 7 — 12a: 1,000		
b	Divide line 5 by line 12a. Enter the result as a decimal (rounded to two places)	12b	× .20
13	Multiply line 11 by line 12b ►	13	56
Step 3	**Figure child's tax**—If lines 4 and 5 above are the same, enter -0- on line 15 and go to line 16.		
14	Subtract line 5 from line 4 — 14: 650		
15	Tax on line 14 based on the **child's** filing status. See instructions. If from Capital Gain Tax Worksheet, enter amount from line 4 of that worksheet here ►	15	99
16	Add lines 13 and 15	16	155
17	Tax on line 4 based on the **child's** filing status. See instructions. If from Capital Gain Tax Worksheet, check here ► ☐	17	129
18	Enter the **larger** of line 16 or line 17 here and on Form 1040, line 38; Form 1040A, line 23; or Form 1040NR, line 37 ►	18	155

Form 8615–Worksheet

Child's name shown on return: Bill Brown — Child's social security number: 0XX : 11 : 1111

A Parent's name (first, initial, and last). Caution: See instructions on back before completing: Tom Brown — B Parent's social security number: XXX : 11 : 1X11

C Parent's filing status (check one): ☐ Single ☑ Married filing jointly ☐ Married filing separately ☐ Head of household ☐ Qualifying widow(er)

Step 1	**Figure child's net investment income**		
1	Enter child's investment income, such as taxable interest and dividend income. See instructions. If this amount is $1,300 or less, **stop**; do not file this form	1	2,100
2	If the child DID NOT itemize deductions on Schedule A (Form 1040 or Form 1040NR), enter $1,300. If the child ITEMIZED deductions, see instructions	2	1,300
3	Subtract line 2 from line 1. If the result is zero or less, **stop**; do not complete the rest of this form but ATTACH it to the child's return	3	800
4	Enter child's **taxable** income from Form 1040, line 37; Form 1040A, line 22; Form 1040NR, line 36	4	1,450
5	Enter the **smaller** of line 3 or line 4 ►	5	800
Step 2	**Figure tentative tax based on the tax rate of the parent listed on line A**		
6	Enter parent's **taxable** income from Form 1040, line 37; Form 1040A, line 22; Form 1040EZ, line 6; Form 1040NR, line 36; Form 1040NR-EZ, line 13. If the parent transferred property to a trust, see instructions	6	52,000
7	Enter the total net investment income, if any, from Forms 8615, line 5, of ALL OTHER children of the parent identified above. **Do not** include the amount from line 5 above	7	200
8	Add lines 5, 6, and 7	8	53,000
9	Tax on line 8 based on the **parent's** filing status. See instructions. If from Capital Gain Tax Worksheet, enter amount from line 4 of that worksheet here ►	9	9,634
10	Enter parent's tax from Form 1040, line 38; Form 1040A, line 23; Form 1040EZ, line 10; Form 1040NR, line 37; Form 1040NR-EZ, line 14. If from **Capital Gain Tax Worksheet**, enter amount from line 4 of that worksheet here ►	10	9,354
11	Subtract line 10 from line 9. If line 7 is blank, enter on line 13 the amount from line 11; skip lines 12a and 12b	11	280
12a	Add lines 5 and 7 — 12a: 1,000		
b	Divide line 5 by line 12a. Enter the result as a decimal (rounded to two places)	12b	× .80
13	Multiply line 11 by line 12b ►	13	224
Step 3	**Figure child's tax**—If lines 4 and 5 above are the same, enter -0- on line 15 and go to line 16.		
14	Subtract line 5 from line 4 — 14: 650		
15	Tax on line 14 based on the **child's** filing status. See instructions. If from Capital Gain Tax Worksheet, enter amount from line 4 of that worksheet here ►	15	99
16	Add lines 13 and 15	16	323
17	Tax on line 4 based on the **child's** filing status. See instructions. If from Capital Gain Tax Worksheet, check here ► ☐	17	219
18	Enter the **larger** of line 16 or line 17 here and on Form 1040, line 38; Form 1040A, line 23; or Form 1040NR, line 37 ►	18	323